



Reference: AUD-7-1: 31 (1491 /03)

Date: 28 November 2003

To: Mr. Ramiro Lopes da Silva,
Humanitarian Coordinator, UNOHCI

From: Uwe Hain, Officer-in-Charge
Internal Audit Division 1, OIOS

A handwritten signature in black ink, appearing to read "Uwe Hain", written over the printed name in the "From" field.

Subject: OIOS Assignment No. AF2003/21/4: UNOHCI liquidation – Procurement issues

1. OIOS conducted a review of the procurement activities within the United Nations Office of the Humanitarian Coordinator for Iraq (UNOHCI) to assess the remaining liquidation tasks and to ensure that all related procurement retrenchment activities are addressed. Consequently, the review focused on issues relating to UNOHCI's liquidation rather than on the overall procurement process. The audit was based upon a review of work programmes, procurement case files, and the follow-up of liquidation tasks within the Mission, as well as interviews with the responsible officials of UNOHCI. The audit was conducted in accordance with the standards for the professional practice of internal auditing in United Nations organizations.

2. The audit identified no improprieties, but did note certain weak internal controls regarding the Mission's procurement activities. Also, improved coordination between the Mission's sections would have resulted in a more prompt cancellation of outstanding orders. Critical delays or the absence of the Receiving and Inspections reports (R&Is) had prevented the Mission's Procurement Section from closing outstanding cases. Furthermore, the high incidence of manual requisitions, purchase orders (POs) and R&Is not captured in the electronic procurement records ("Reality", "Mercury" databases) also led to the absence of an adequate audit trail. Finally, there were some instances where delays were directly attributable to the Procurement Section's failure to address outstanding cases on time.

3. We would appreciate receiving your comments concerning our recommendations by 12 December 2003.

Procurement Liquidation Planning

4. Procurement activities during the liquidation phase relate primarily to the closure of pending orders or requisitions that did not materialize in POs, termination of ongoing contracts, including lease agreements, and final settlement of invoices. Chapter Six of the Field Mission Liquidation Manual spells out the following tasks associated with procurement retrenchment activities: (i) requisitions, which at the time of liquidation have not resulted in a contract or purchase order must be cancelled, with the exception of justifiable requirements for goods and services that will be

required during the liquidation period, (ii) partially satisfied requisitions should be reviewed to determine whether the remaining goods or services are still required, (iii) formal termination notices should be issued to the contractors, landlords of rented facilities and owners of rented equipment, and (iv) open-ended supply contracts should be reviewed with a view to (a) satisfying contractual obligations in terms of minimum purchase quantity and renegotiating terms in the best interest of the United Nations, or (b) cancelling the arrangements at no cost.

5. The Procurement Section submitted its Liquidation Work-Plan on 8 July 2003, according to the Chief Administration Officer's Memorandum of Instruction – Mission Winding Down and Liquidation of 16 June 2003. However, the Plan only listed general liquidation tasks without an indication of the workload and associated timeframes. Subsequently, as part of the Weekly Implementation Report mechanism, the Procurement Section submitted to the Liquidation Team more detailed information on outstanding procurement cases. OIOS calculated that as of 31 October 2003, approximately \$800,000 was outstanding with respect to incomplete procurement actions. The Mission advised that there were no instances where requisitions had not resulted in POs.

6. It should be noted that for several months the Mission provided support to the United Nations Assistance Mission in Iraq (UNAMI). As part of the liquidation process, it was intended that some of the outstanding cases, notably construction projects, service contracts and lease agreements would be handed over to UNAMI. Consequently, a memo was sent on 16 September 2003 seeking advice on the possible roll-over and/or transfer of pending contracts to UNAMI, for which a reply was only received on 22 October 2003.

Construction projects

7. At the time of the audit, some progress had been made to clear balances related to construction projects. As of 31 October 2003, there was an outstanding balance of approximately \$250,000. By 7 November 2003, the balance had been reduced to \$207,580. However, OIOS found that all of the outstanding cases related to the construction projects should already have been cleared by the Procurement Section and the balance reduced accordingly. An updated summary of outstanding construction projects as of 11 November 2003 is shown in Table I below:

Table I

	PO No. PO Date	Value \$	Description	Remarks
1	CYP/104 10/06/03	\$156,585	Construction of security fence	UNAMI provided a revised and reduced scope, contract being finished under UNOHCI agreement. Revised PO raised on 20 October 2003.
2	PO2-376 31/10/02	28,990	Construction of gymnasium and upgrades	Invoice and R&I for 5.6 percent completed work in March 2003.
3	POB3-72	14,700	Internal painting	Partially executed - Pending receipt of invoices and R&I for completed work.
4	CYP/134 27/05/03	4,650	Construction of protection wall	Never executed. UNAMI initiated a new wall project.
5	CYP/144	2,655	Construction of generator house	Partially executed - Pending receipt of invoices and R&I for completed work.
TOTAL		\$207,580		

8. The largest outstanding balance is represented by the Sarmed Engineer Office in respect of fencing the UNOHCI Headquarters complex. According to the PO raised on 10 June 2003, the construction work should have started immediately after the receipt and acceptance of the PO by the vendor, with the entire project to be completed within sixty days. The PO further stated that 95 per cent of the contract value would be paid upon completion of the work and certification by the Chief, General Services Section (CGSS), with the remaining five percent payable after the six-month agreed upon warranty period. However, the audit found that on 14 August 2003, an amount of \$50,693 was paid for partial work based on a memo from the Procurement Section. The R&I report dated 13 August 2003 stated various stages of completion ranging from nil to 55 per cent. It should also be noted that the R&I report and the related invoice were certified by a Building Management Services assistant instead of the CGSS or an alternate.

9. During October 2003, an agreement was reached between UNAMI and UNOHCI regarding the closure of the above contract. UNAMI agreed upon a reduced scope of work, provided that the contract was terminated under UNOHCI's arrangements. On 20 October 2003 an amended PO amounting to \$91,645 was raised by UNOHCI for construction projects to be completed within sixty days. It should also be noted that a second payment of \$28,666 was made on 5 November 2003 covering 70 per cent of the above-referenced project, leaving an unliquidated balance of \$12,286. Since the construction projects will extend one month beyond the Mission's closure date of 21 November 2003, in OIOS' view, all the construction contracts and related balances should have been transferred to UNAMI.

10. During 2002, the Mission entered into a contract of \$28,990 with Abu Khalid Bureau for the

construction of a gymnasium and upgrades of the kitchen at the Canal Hotel Headquarters. The PO issued on 31 October 2002 stated that the work should be completed within 40 days after acceptance. A partial payment of \$1,623 was made on 11 March 2003, although less than six per cent of the work had been completed and the contract did not call for partial payment. Furthermore, the contract stipulated a penalty of up to 10 per cent of the contract value for each week of delay until completion of the work. As of the date of the review, no further construction work had been done, and there is an outstanding balance of \$27,367.

11. The remaining outstanding contracts refer to instances of partially executed contracts for which no R&I reports and invoices from the contractors exist. Furthermore, one contract signed in May 2003 was never started. However, all these matters appear as outstanding on the Mission's books even though the Mission is approaching closure. Although OIOS' review found that some of these cases had in fact already been closed, the audit team found unreasonable delays in respect of the closure of the actions and their related balances. Some delays were due to the lack of R&I reports certifying the completion stage, while others were a direct consequence of the Procurement Section's tardiness. For example, it took the Procurement Section five months to close the outstanding contract CYP/082 with Al-Kamal Shop for the installation of air-conditioning units.

12. OIOS's review also found two instances where POs were raised after the receipt of invoices from the contractors (POB3-48 and POB3-57). Furthermore, one payment of \$3,335 in respect of one of the POs was disbursed on 9 March 2003 without an R&I report.

13. It should also be noted that on 28 August 2003, one of the contractors submitted a claim seeking damages amounting to \$4,000 for the destruction of construction materials and equipment. The Mission's Legal Adviser provided a legal opinion related to the appropriateness of the alleged claim under the force majeure provisions of the pertinent PO. No formal response has yet been sent by the Mission.

Recommendations 1 to 3

UNOHCI should:

- (i) Transfer the remaining work to be performed under Purchase Order UNOHCI/CYP/104 to UNAMI and close the remaining balance of the project (AF03/21/4/001);
- (ii) Immediately initiate the closure of all remaining outstanding construction projects (AF03/21/4/002); and
- (iii) Take steps to provide a resolution with respect to the contractor's claim of \$4,000 as damages for the loss of construction materials (AF03/21/4/003).

Recurring service and supply contracts

14. The outstanding procurement activities related to the recurring service and supply contracts amounted to approximately \$140,000 as of 11 November 2003. An updated summary of the status of these contracts is shown in Table II below:

Table II

PO No.	O/S Value \$	Description	Remarks
1 PROC/03-001	\$72,628	Provision of meals	No action taken by the Administration to settle the advance disbursed to the Contractor.
4 CYP/140	12,769	Repair of three ambulances in Amman, Jordan	Pending receipt of invoices and R&Is. Two ambulances were repaired. An amended PO was raised on 4 November 2003 to cover the costs for the third ambulance.
2 POB3-075	14,195	Cleaning services at the Canal HQ	To be taken over by UNAMI.
3 POB3-073	9,232	Maintenance services at the Canal HQ	To be taken over by UNAMI.
5 POB3-014	2,295	Supply of spare parts for the Transport workshop in Baghdad	No action taken to close the redundant contract.
6 PO2-108	1,942	Re-winding of electrical motors in Baghdad	No action taken to close the redundant contract.
6 Others	27,161	Customs clearance, freight, office supplies, vehicles' rental, etc	Supply and service contracts for day-to-day activities.
TOTAL	\$140,222		

15. The largest outstanding balance is represented by the Al-Finjan Restaurant in the amount of \$123,844.50. This balance relates to a contract for the provision of meals to the Government of Iraq Guards Contingent, from 1 January through 31 December 2003. An advance payment of \$31,216 was disbursed to the contractor on 17 March 2003 in view of the prevailing conditions in Iraq at that time. The advance payment was duly approved by the Controller of the Mission on 5 March 2003 based on an amendment to the original contract. An additional payment of \$20,000 was also made. The amendment to the contract stipulated the provision of dry food for two months under the management and supervision of the UNOHCI Interim Administrative Team. It should be noted that the amendment

to the contract did not contain any reference to the amount to be disbursed to the contractor. Furthermore, the advance that was disbursed covered three months as opposed to the two months specified in the amendment to the contract. During July 2003, the contractor submitted six invoices totaling \$11,741. Although the Mission's administration could not confirm the quantities delivered, a memo dated 29 October 2003 was sent to the contractor requesting reimbursement of \$19,475, representing the difference between the advance payment disbursed to the contractor on 17 March 2003 and the six invoices submitted by the contractor.

16. It should also be noted that, according to the opinion provided by UNOHCI's Legal Advisor on 6 September 2003, advance payment terms stipulated in the amendment to the contract with the Al-Finjan Restaurant appear inconsistent with the original contract. Therefore, according to the opinion, it is "no longer mandatory for payments to the Contractor to be monitored against certified invoices with supporting documentation". The legal opinion also recommends that the Mission should use "the best endeavors in reaching an amicable settlement by seeking for a reimbursement of a proportionate amount as a refund of the advance made on the basis of a good faith contractual relationship at a time of exigency". The audit noted that, except for the request for reimbursement sent to the contractor on 29 October 2003, no steps had been taken by the Mission's administration to settle the case.

17. As part of the winding down process, the CAO instructed the CGSS in June 2003 to identify the point in time where services provided to the mission, including cleaning and maintenance of the premises, fell below 20 per cent and to submit a cost proposal accordingly. However, the cost proposal never materialized even though the cleaning and maintenance services for the Canal Hotel Headquarters clearly fell below the 20 per cent threshold. The Mission continued to incur monthly expenses at the full rate for cleaning services in September and October. UNAMI has expressed an interest in taking over these service contracts, but no subsequent action had been taken by the Mission's administration.

18. Two small contracts related to the supply of miscellaneous items for the transport workshop and re-winding of electrical motors remain valid up to 31 December 2003, although no requirements have materialized since March 2003.

Recommendations 4 to 6

UNOHCI should:

- (i) Take steps to reach a settlement with the Al-Finjan Restaurant by seeking the reimbursement of a proportionate amount of the advance payment of \$31,216 disbursed to the contractor (AF03/21/4/004);
- (ii) Immediately liquidate the outstanding balances in respect of the maintenance and cleaning services and hand over the contracts to the UNAMI administration

(AF03/21/4/005); and

(iii) Immediately liquidate the outstanding balances related to the supply contracts (AF03/21/4/006).

Termination of lease agreements

19. During the active life of the Mission, the administration entered into a series of lease arrangements for various units scattered within Iraq, as follows: 12 in Erbil, 5 in Dohuk and 1 each in Diana, Suleimaniyah, and Zakho, with a cumulative monthly rental cost of \$11,500. Most of the leases expire on 31 December 2004, except for two units in Dohuk expiring on 31 December 2003, and one unit in Suleimaniyah expiring by 30 September 2005.

20. Beginning October 2003, UNAMI informed UNOHCI that it would not have any presence in Dohuk, but would have a presence in the five following locations: Basra, Erbil, Hillah, Mosul and Suleimaniyah. UNAMI further indicated on 22 October 2003 that a single office would be required in each of the five areas. Moreover, the locations would be subject to the Deputy Humanitarian Coordinator's assessment.

21. As of the date of this review no decision to terminate any lease arrangements has been taken by the Mission's administration. It should be noted that all the lease agreements require thirty days written termination notice, or one month's rent in lieu of notice. Since the Mission's closure is set for 21 November, the lack of action has translated into unnecessary expenditure and that are likely to accumulate as the "one month's rent in lieu of notice" option is exercised. Even though lease terminations could have been initiated at the beginning of October for the Diana, Dohuk, and Zakho units, no action had yet been taken by the Mission's administration. Furthermore, on 16 September 2003, the Mission entered into a new lease agreement in Dohuk for the period from 16 September to 31 December 2003.

Recommendation 7

UNOHCI should:

(i) If possible, seek to turn over its leased unit in Suleimaniyah and one of its leased units in Erbil to UNAMI; and

(ii) Immediately initiate the termination of its remaining lease agreements (or of all leases if the turnover to UNAMI is not possible), to ensure that no additional unnecessary expenditures are incurred beyond the closure date of the Mission (AF03/21/4/007).

Termination of procurement activities

19. During September 2003, all 115 international vendors were notified of the closure of UNOHCI and requested to review their outstanding balances with the Mission. The exercise did not include any local vendors in Iraq.

20. As part of the procurement retrenchment, the Mission endeavored to clear its backlog of pending international procurement cases, especially the consignments accumulated in Amman, Jordan. The latter included those accumulated prior to the war when a MOFA Iraq clearance was required for goods before being shipped into the country. At the time of OIOS' review, the outstanding consignments in Jordan amounted to approximately \$180,000. However, by the end of October, all consignments were shipped to Iraq. OIOS's review found that six POs with a cumulative value of \$50,000 were not reported as outstanding as part of the liquidation Weekly Implementation Report. Even though all procurement cases were subsequently cleared, failure to include them in the tracking platform of the liquidation progress indicated a weak monitoring mechanism.

22. There were also inconsistencies in the pricing of communication equipment that resulted in overcharges of approximately \$5,000 in respect of PO No. UNOHCI/CYP/037. On 1 May 2003, the Mission's administration issued a PO for \$181,923 for sixty transceivers and related accessories from Barrett Europe Ltd. The United Nations has a system contract with the vendor and "agreed upon" prices for communication equipment stipulated in amendment two to PD/C0113/00 of 27 December 2002. All prices in the amendment are quoted in Australian dollars. However, on 25 April 2003, UNOHCI received a quotation in United States dollars that was the basis for the Local Committee on Contracts' deliberations and subsequent issuance of the PO. By converting the "agreed upon prices" on the system contract to the "quotation prices", and using the relevant foreign exchange rates, there was an overcharge of approximately \$5,000 for the total order. It should be also noted that amendment two to the system contract contains a provision stipulating that "each invoice paid by the UN or the Agencies shall be subject to a post-payment audit by the UN or the Agencies' auditors" and that the "UN may be entitled to a refund from the contractor for any amounts shown by such audits."

23. OIOS's review also identified serious procurement flaws with respect to two instances concerning the storage and transportation of UN vehicles from Jordan to Iraq. The PO CYP/188 amounting to \$23,592 was raised on an *ex-post facto* basis on 16 October 2003, to cover the charges incurred to store 33 vehicles from July 2002 to April 2003, including custom clearance and handling charges. The UNOHCI freight forwarding contract with the vendor Maltrans Shipping Agencies expired on 31 August 2002, and the Procurement Section was not aware of any arrangements related to the vehicles. Furthermore, it took more than ten months for the Transport Section to raise a requisition to justify the requirements and to obligate funds. Similarly, the Mission entered into a contractual arrangement with Eastern Service Company in Amman, Jordan, completely bypassing the Procurement Section. The PO CYP/188 was also raised on a *post facto* basis on 16 October

20003 to cover the charges of \$15,551 incurred by the transportation of 11 vehicles to Iraq in May 2003. Even though these procurement cases were closed and they do not involve sizeable amounts, they evidence major departures from the established procurement procedures. The serious breaches of internal controls were made possible by a lack of coordination by the sections involved in these activities.

Recommendation 8

UNOHCI should establish a receivable covering the overcharge of \$5,000 paid to Barrett Europe Ltd and initiate a recovery action (AF03/21/4/008).

Closure of the procurement files in the Mercury System

24. Beginning January 2003, the Mission's procurement database migrated from the "Reality" to the "Mercury" System. Because of the Mission's subsequent relocations, many of the procurement documents were raised manually and were never captured in the electronic databases. Consequently, the Mercury database is neither complete nor accurate.

25. The auditors identified three scenarios that departed from the established electronic procurement cycle, as follows: (i) electronic Requisition - electronic PO - manual R&I, (ii) electronic Requisition - manual PO - manual R&I, and (iii) manual Requisition - manual PO - manual R&I. In the first category, a number of manual R&I reports were issued from the three Northern Governorates, as well as Amman, Jordan and Larnaca, Cyprus. However, some of the manual R&Is were entered in the Mercury System and the updating process is in progress. During 2003, approximately 200 POs were manually raised, out of which approximately 90 percent fell under the third category. The high incidence of manual Requisitions, POs and R&I reports not captured in the Mercury database prevented the development of a reasonable audit trail both for the Procurement Section and the administration. Capturing all manual records into the electronic procurement cycle represents a time-consuming exercise, but the benefits of such an exercise should be carefully examined by the Mission's administration.

Recommendation 9

UNOHCI should enter all manual procurement documentation, including requisitions, purchase orders and receiving and inspection reports, into the Mercury electronic database system (AF03/21/4/009).

26. I take this opportunity to thank the management and staff of UNOHCI for the assistance and cooperation provided to the auditors in connection with this audit segment.

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